No. 18,413

United States Court of Appeals

For the Ninth Circuit

ROSENBERG BROTHERS & COMPANY, INC., a corporation, and ARNOLD-HOOVER INCORPORATED, a corporation,
Appellants,

vs.

ALBERT ARNOLD,
Appellee.

and

ALBERT ARNOLD,
Appellant,

vs.

ROSENBERG BROTHERS & COMPANY, INC., a corporation, et al.,
Appellees.

Appeals from the United States District Court for the Northern District of California, Southern Division

APPELLANTS' REPLY BRIEF

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APPELLANTS' REPLY BRIEF

I

APPELLEE'S OWN BRIEF DEMONSTRATES THE VALIDITY OF OUR CONTENTION THAT THE PORTION OF THE JUDGMENT AWARDING $23,677.40 AS 50% OF THE ALLEGED PROFITS OF ARNOLD-HOOVER, INC. MUST BE REVERSED.

At pages 5-15 of our Brief for Appellants we set forth the reasons why that portion of the judgment

awarding $23,677.40, representing 50% of the alleged profits of Arnold-Hoover, Inc., must be reversed in view of the extraordinary state of the record.

It was pointed out that two documents constituting the only evidence on the subject of profits or losses of Arnold-Hoover, Inc. (Defendants' Exhibit L and Plaintiff's Exhibit 213) both showed that the net income (loss) as computed for Federal income tax purposes was a loss of $15,677.81, so that no payment for profits was due Arnold.

Appellee Arnold attempts to answer this argument at pages 11-18 of his Brief, but the effort only serves to demonstrate more emphatically the validity of our position. A careful reading and analysis of Arnold's argument will convince the reader that our contention on this point must be sustained, and at least this portion of the judgment reversed.

1. **Appellee Arnold, who had the burden of proof, contents himself with the argument that "respondent wholly ignored the issue in presenting its evidence."**

Arnold was the plaintiff (appellee now). It was he who sought relief in the form of damages. His was the burden of proof—both as to the existence of profits and on other issues.

Yet, with the deficiency in his evidence exposed in our Appellants' Brief (pp. 5-15) he contents himself with relying upon an argument characterized by the statement that:

> "*Appellants presented no testimony as to the existence or non-existence of operating profits.*" (Emphasis added.) (Appellee's Brief, p. 12.)

Lacking any evidence on his own that will sustain either his burden of proof or this portion of the judgment, appellee's whole argument is characterized by these additional selections from page 12 of his Brief:

1. "Robert Moore, secretary-treasurer of Rosenberg, was called as a witness. . . . but *gave no testimony on this issue.*" (Emphasis added.)

2. "*Appellants called no witnesses* from the firm of independent accountants." (Emphasis added.)

3. "In short, *Rosenberg completely ignored the issue at the trial,* and presented no evidence disputing the amount of the profits on which the bonus was based." (Emphasis added.)

Can it be that they have overlooked the fact that Rosenberg was a defendant, who had no responsibility to call anyone or prove anything unless and until Arnold had first proceeded with his initial burden of proof—which he never did?

2. Failing to point out any evidence that will support this portion of the judgment, appellee merely attempts to shift the burden of proof on the issue of alleged profits.

The law is clear in California that a promise by a defendant to pay plaintiff out of profits is a conditional obligation to pay, and that before plaintiff can recover any damages under such a contract, he must allege and *prove* that the condition has been complied with. (Emphasis added.)

Van Buskirk v. Kuhns (1913) 164 Cal. 472;
Draper v. Patterson (1958) 156 C.A. 2d 606, 608-609.

Under this rule Arnold had the burden of proving by a preponderance of the evidence that Arnold Hoover, Incorporated, actually earned "net operating profits", as that term is defined in the contract, for the year July 1, 1957 to June 30, 1958. The contract defined "net operating profits" in clear, certain and unambiguous terms, as follows (Tr. 14):

> "The net operating profits of Arnold-Hoover Incorporated, shall mean its net income as computed for Federal income tax purposes, excluding all gains and losses from capital transactions and excluding also that portion of the profit realized upon liquidation of its LIFO inventory existing at the close of business February 28 1955, which represents the difference between such LIFO value and the cost or market value of such inventory used in computing the price paid by Rosenberg to stockholders of Arnold Hoover, Incorporated, in acquiring the stock of Arnold-Hoover, Incorporated, as of the close of business February 28, 1955. Payment of such compensation to Arnold by Arnold-Hoover, Incorporated, shall be made for each fiscal year after the final operating results for the particular fiscal year of Arnold-Hoover, Incorporated shall have been audited by the certified public accountants to be retained by Rosenberg and by Arnold-Hoover, Incorporated."

To argue, as does Arnold, that Rosenberg "wholly ignored the issue [of the profits of Arnold-Hoover Inc.] in presenting its evidence" (Appellee's Brief p. 12), is simply a desperate attempt to shift the bur

den of proof to Rosenberg to disprove that Arnold-Hoover, Incorporated, realized "net income as computed for Federal income tax purposes, excluding all gains and losses from capital transactions". Such an effort is contrary to the law as stated in *Draper v. Patterson, supra,* and is without merit.

3. Arnold failed to sustain the burden of proving that Arnold-Hoover, Incorporated, realized "net operating profits for income tax purposes".

In *Draper v. Patterson* (1958) *supra,* 156 C.A. 2d 606, plaintiff commenced an action to recover damages for breach of contract. The contract provided that plaintiff was to clear and level land for defendant and he was to be paid by defendant "from the profits of crops off the land now being cleared". After trial, judgment was rendered for plaintiff. On appeal, the District Court of Appeal reversed the judgment on the ground that there was no evidence to sustain the finding of the existence of "profits". In this connection the Court stated as follows (156 C.A. 2d 609-610):

> "Defendant next contends that there is no evidence in the record to sustain a finding of profit. *While there is evidence to indicate that a profit may have been made from the lands in question, there is no evidence whatsoever as to the amount of said profit if any.* The land cleared was in three separate parcels referred to as the west field, the south field and the north field. The west field was planted to barley and rye in 1953 and 1954, and defendant's cattle were permitted to feed off the crop. The south field was planted

to milo in 1958 and fed off to the cattle, and in 1954 it was planted to oats and was also fed off to the cattle. The north field was planted to sudan grass in 1954 and oat hay in 1955. Some of the hay was traded for corn feed. There is no evidence as to the value of the pasturage in question or the value of any of the crops which were produced or as to the amount thereof, or as to what if any profit was made from any of the particular crops. *These are matters which should have been proven in order to support the judgment, since the contract provided that defendant was to pay for the work out of profits from crops produced on the lands in question.* The fact that defendant farmed the lands in question and beneficially used them does not necessarily indicate that he made a profit from any crops produced on said lands. It is obvious that one may use a thing without making a profit. *It is also clear from a reading of the record in this case that when the parties were negotiating the contract they were using the term 'profit' to mean the excess in value over the cost of producing the crop or crops that were considering the profits or loss from the particular land in question, not from the operation of the ranch as a whole. We conclude that the evidence is insufficient to sustain the judgment."* (Emphasis added.)

The Court's reasoning is equally applicable to Arnold's claim that Arnold-Hoover, Incorporated, realized net operating profits for the 1957-1958 fiscal year, which are defined in the contract as "net income as computed for Federal income tax purposes, excluding all gains and losses from capital transactions".

4. **The exact nature of the evidence on the issue of alleged profits of Arnold-Hoover, Inc.—and its insufficiency.**

On the issue of alleged profits, the only evidence that Arnold (or anyone else) can point to consists of three items:

1. Defendants' Exhibit L—The document entitled "Rosenberg Bros. & Co., Inc. and Subsidiaries Taxable Income Computations, Year Ended June 30, 1958".

As to Arnold-Hoover, Inc. this exhibit showed: 'Income (loss) per return—[$15,667.89]. *Not profits, but a loss, was proved.*

2. Plaintiff's Exhibit 213—The F. W. Lafrentz & Co. audit of Rosenberg Bros. & Co., Inc., and its subsidiaries dated June 30, 1958, which report also showed the net income (loss) per income tax return to be a loss of $15,677.89. *Again, not profits, but a loss, was proved.*

3. Other than those two documents, both of which proved a loss rather than profits, the only other evidence was the testimony of one Victor B. Staadecker, a partner in a firm of certified public accountants.

At best his testimony was equivocal. It did not prove anything one way or the other. In no way could it be construed as contradicting, criticizing, or qualifying the accounting procedures as audited by F. W. Lafrentz & Co. The Lafrentz audit showed that Arnold-Hoover, Inc. did not realize any net income as computed for Federal income tax purposes, excluding all gains and losses from capital transactions, by reason of its operations in the 1957-1958 fiscal year.

The closest that Staadecker came to offering anything pertinent to the issue will be found in this effort to elicit proof:

> "Q. (By Mr. Bull.) Mr. Staadecker, based upon your experience as a certified public accountant, do you have an opinion as to whether or not, according to generally-established principles of accounting, all gains or losses incurred in the liquidation of a company could be properly classified as gains or losses incurred in capital transactions?
>
> * * *
>
> A. Well, as I stated previously, the transactions in liquidating a corporation in order to get money to retire or redeem its stock are capital transactions, and where the liquidation of the assets of the corporation fit into that picture, *I think they could be classified as capital transactions.*" (Tr. 198-199, emphasis added.)

As will be noted, even on this simple direct examination, Staadecker was equivocal: "I think" and "they could be".

Any doubt as to the nebulous, equivocal nature of Staadecker's contribution was eliminated rapidly by a very short cross-examination:

> "Q. (By Mr. Johnson.) "When you used the term that such transactions, referring specifically to gains or losses incurred in a liquidation of a company, could be listed as gains or losses from capital transactions, *what did you mean when you used the term 'could be'?*
>
> A. Well, in the broad, general sense that you were liquidating a corporation.

Q. You mean in the broad, general sense that *in some instances they might be so classified, in others they might not?*

A. *No, I don't think so. I think that the area in there is not too well defined.*

Q. *You think the area isn't too well defined?*

A. *No.*

Q. Have you personally been confronted in your profession with such situations?

A. Well, to the extent where we have been asked to do things where we have had to ask for a legal interpretation of the contract.

Q. You had to ask for a legal interpretation?

A. Interpretation of the contract.

Q. Did you ask for a legal interpretation of this contract?

A. I didn't, no." (Tr. p. 201, emphasis added.)

This evidence falls far short of sustaining Arnold's burden of proving that all the conditions prerequisite to his right to receive a portion of profits as compensation for managing the Arnold-Hoover, Inc. fig business were met.

First, Arnold did not prove that Arnold-Hoover, Inc. realized net operating profits as defined in the contract, namely, "net income as computed for Federal income tax purposes, excluding all gains and losses from capital transactions".

Arnold simply attempted to go behind the computation of net income for Federal income tax purposes, and sought to quarrel with the accounting procedures used by Rosenberg and F. W. Lafretz & Co., claiming that the liquidation loss charged against operating income "could be" classified as a capital transaction

and thus under the terms of the contract, it "could be" excluded in computing net income.

This same type of argument has been rejected under the reasoning in the *Draper* case, *supra,* where the Court said that the fact there "may" be profits is not sufficient evidence to show that there were profits. And so in this case, the fact that a liquidation loss "could be" classified as a capital transaction is no evidence that it should have been, and in the absence of proof that is certain and unequivocal, Arnold has failed to sustain the burden of proving damages in this connection.

See:

Draper v. Patterson (1958) 156 C.A. 2d 606, *supra.*

Secondly, Arnold failed to introduce any evidence that the condition which could have created Rosenberg's obligation to pay him had been met, namely, proof that the audit report of the operations of Arnold-Hoover, Inc., by certified public accountants retained by Rosenberg by its own terms showed that profits were earned. Under the terms of the contract, compensation for managing Arnold-Hoover, Inc. "shall be made for each fiscal year after the final operating results for the particular fiscal year of Arnold-Hoover, Incorporated, *shall have been audited by the certified public accountants to be retained by Rosenberg and by Arnold-Hoover, Incorporated.*" The audit report, (Plts. Exh. 213) confirms that Arnold-Hoover, Inc. realized no net income for purposes of Federal tax purposes, excluding all gains and

losses from capital transactions, for the fiscal year in question. Arnold did not introduce any evidence that in any way impeaches the validity, accuracy or correctness of the audit report. Consequently, since the audit report stands unimpeached, and since the report without contradiction shows that Arnold-Hoover, Inc. did not realize net income for Federal income tax purposes, excluding gains and losses for capital transactions, there was no duty to pay Arnold any compensation for managing Arnold-Hoover, Inc.

5. Proper interpretation of the contract: The terms "gains and losses from capital transactions" and "liquidation" are mutually exclusive.

In the absence of any pertinent and relevant evidence to sustain the judgment awarding him damages for managing Arnold-Hoover, Inc., Arnold attempts to interpret the contract so as to supply the missing evidence. (Appellee's Brief, pp. 14-17.)

Arnold's argument that it is contrary to the intent of the parties to construe the term "net operating profits" (which the contract defines as "net income for Federal income tax purposes, excluding all gains and losses from capital transactions") as permitting a liquidation charge, will not stand analysis.

Paragraph 7 of the contract as quoted above, clearly shows an intent by the parties to treat "capital transactions" and "liquidation transactions" as mutually exclusive and different from one another. Paragraph 7 in this connection reads as follows:

> "The net operating profits of Arnold-Hoover, Incorporated, shall mean its net income as com-

puted for Federal income tax purposes, excluding all gains and losses from capital transactions, *and excluding also that portion of the profits realized upon liquidation of its LIFO inventory existing at the close of business February 28, 1955.*" (Emphasis added.)

The inclusion of the italicized clause above shows that the parties did not regard "liquidation transactions" as included in the clause "capital transactions". Since the contract expressly recognizes both types of accounting procedures and distinguishes between them, and since Arnold had full knowledge of this distinction, he cannot now be heard to contend that a "liquidation" transaction was intended to be classed as a "capital" transaction.

The argument that the provision for compensation for managing Arnold-Hoover, Inc. induced Arnold to give up his business is no more relevant to the interpretation of the employment contract than the fact that Consolidated Food Corporation purchased Arnold's fig brokerage business (Arnold-Hoover Company) for $100,000. (Plts. Exh. 1.) Arnold's rights were governed by the contract and, if as Arnold states in his brief, he accepted employment by a company "which was definitely going down hill" (Appellee's Br., p. 17), he was on notice that the company might not continue in business for the full term of his contract and might in fact liquidate.

6. The authority cited by appellee is not controlling.

The case cited by Appellee on page 16 of his brief, *Crillo v. Curtola,* 91 Cal. App. 2d 263, 204 Pac. 2d

941 (1949), is not applicable to this case, since *Draper v. Patterson, supra,* is controlling.

The *Crillo* case is distinguishable on its facts. In that case defendant made no contention that plaintiff had failed to present sufficient evidence to support the finding of damages and the key issue determined by the Court was the duties required of plaintiff under the contract.

7. **Conclusion: This portion of the judgment must be reversed.**

For the foregoing reasons and those stated in Appellants' Opening Brief, pages 5-15, that portion of the judgment awarding appellee Arnold $23,677.40, as representing 50% of the alleged profits of Arnold-Hoover, Incorporated, cannot be sustained and must be reversed.

II

THE FINDINGS OF THE TRIAL COURT THAT ARNOLD DID NOT BREACH HIS FIDUCIARY DUTY, DID NOT DISOBEY DIRECTIVES OF THE BOARD OF DIRECTORS, AND DID NOT NEGLIGENTLY PERFORM HIS DUTIES ARE CLEARLY ERRONEOUS AND MUST BE REVERSED BECAUSE A REVIEW OF THE ENTIRE EVIDENCE LEAVES A DEFINITE AND FIRM CONVICTION THAT A MISTAKE HAS BEEN COMMITTED.

1. **Scope of review of findings of fact and conclusions of law on appeal.**

Appellee Arnold in his Brief, states that he accepts the position that "the existence or non-existence of . . . substantial evidence upholding the Trial Court's finding . . ." is reviewable, and that a finding may not be set aside" . . . unless there is no substan-

tial evidence to sustain it, unless it is against the clear weight of the evidence, or unless it was induced by an erroneous view of the law." Appellees' Br., p. 6.)

Appellee Arnold also agrees that *United States v. United States Gypsum,* 333 U. S. 364, 394-395, 69 S. Ct. 525, 92 L. Ed. 746 (1948) is correctly cited as a leading case in the area of appellate review, and that he will "accept the test quoted by appellants" (B. 18)." (Appellee's Br., p. 7.)

Accordingly, in view of these very major concessions by Appellee, there is no dispute as to the Court's reviewing powers in this case. Consequently, the evidence herein is to be reviewed in light of the test set forth in *United States v. United States Gypsum, supra,* and as elaborated in *Orvis v. Higgins* (1950, C.A. 2d) 180 F. 2d 537, 538, cert. den. (1950) 340 U.S. 810, 71 S. Ct. 37.

Arnold seeks to show that there is much oral testimony in the record to support the judgment that he was not negligent, or that he did not disobey directives, or that he did not breach his fiduciary duty. However, in reality this oral testimony is merely the statement of Arnold's memory of the past events that occurred during his employment by Rosenberg. But, where these same past events are recorded in documents executed contemporaneously with the events themselves, the Court is not required under the above rules of appellate review, to accept Arnold's version of these facts, since it can review the documents itself and make its own inferences from them.

A review of this uncontradicted documentary evidence, recording events simultaneously, leaves anyone reviewing the evidence with the definite and firm conviction that a mistake has been committed by the trial Court in concluding that plaintiff was not negligent, did not disobey directives, and did not breach his fiduciary duty.

2. There are "normal practices" in the fig industry.

In Appellee's Brief (page 20) Arnold agrees that the expert witnesses all testified that it was not normal to store figs for more than two years, but he then attempts to interpret this evidence as saying that the witnesses really did not mean that there are "normal practices" in the fig industry. This attempt to pervert the meaning of what these expert witnesses stated is sought to be justified on the ground that not every fig packer adheres to the principle of not storing figs for more than two years.

This argument discloses that Arnold has misconstrued what is meant by normal practices. The word "normal" does not mean, as Arnold would have us believe, what every packer in fact does, but instead it is defined as constituting the established norm, standard, rule, or principle, that it is the average or the mean.

See:

66 C.J.S. Normal, p. 606;

U. S. v. Fallbrook Public Utility Dist., D.C. Cal. 109 F. Supp. 28, 38.

The fact that various packers may have deviated from the normal practice of storing figs does not mean there was no standard in the fig industry for storing figs. It only means that this standard was being violated, and does not in any way detract from the fact that there were and are normal practices which are recognized by persons in the fig industry for storing figs.

Arnold in his Brief (page 22) in effect agrees with this position, stating "it is clear that everyone recognized the desirability of disposing of figs within two years. This was the practice which, under ordinary conditions, the packers would strive to observe."

After making this admission and concession, Arnold argues that the normal practices for storing figs could no longer serve to measure storage time for figs because during the years in question there were abnormally big fig inventory carry-overs. What Arnold overlooks is that the normal practice for storing figs is based upon the fact that figs, being a perishable commodity, deteriorate with age, so that after two years the market value decreases. This was made clear by the testimony of C. F. Fisher, who stated that certain of the old crop figs stored under Arnold's direction had suffered a loss in market value, as follows:

> "Q. I now show you 1955 crop Blacks from Box B-27.
>
> A. This one, the color degradation has gone farther, and such figs would have little value for juice . . .
>
> * * *

A. . . . All these Black figs that are there can be sold. I think the price probably would be affected.

Q. How would it be affected? Would it be lower or higher?

A. *It would be lower. That is, it wouldn't bring what the current crops would."* (Tr. 467-468.)

"Q. . . . I now show you a box entitled, B-4, 1956 crop Calimyrnas.

A. These are figs that were then nearly eighteen months old at the time I sampled them. Some darkening has taken place. You could make commercial pack out of it, but you would have to do some sorting. *The downgrading pricewise would not be extensive.*

* * *

Q. And you say the market for the 1956 crop figs would be reduced?

A. *Well, I would put it this way, rather, that in the 1956 crop you would need some considerable sorting, which is a costly thing, because the sort outs are downgraded. If it were to be packed into a consumer pack."* (Tr. 468-469.)

"Q. I show you now Box 1, on which is written 100 tons, 1955 crop Adriatics.

A. *These are degraded to the point where I, in my judgment—they could not be salvaged . . .*

Q. What do you mean when you say beyond salvage?

A. For human food. In my opinion, the only outlet would be as cattle feed or hog feed." (Tr. 469-470.) (Emphasis added.)

Mr. Fisher's testimony with regard to the 1954 and 1955 crop Adriatics, and 1954, 1955 and 1957 crop

Kadotas, was in substance the same as quoted above, which is to the effect that the figs sampled would to a greater or lesser extent have decreased in market value.

It is evident that the normal practice in the fig industry not to store figs over two years is based on the obvious fact that any storage over two years causes a drop in the market value of the figs stored.

Consequently, the fact that there were abnormal years in the fig industry because there were large fig inventory carryovers, would not in any way justify storing figs over two years, since 1,000,000 pounds of 1955 crop fig inventory still would be worth less in 1958 than it was in 1957. Abnormally large fig carry-overs will not result in increasing the market value of the figs, but only in decreasing such value. It follows that to lessen the loss from continual depreciation due to age, the fig inventory should be sold before it is stored over two years.

The fact that the fig industry may be volatile and speculative, is not helpful to Arnold's case. If figs stored over two years decrease in market value, the only question is how much is the decrease. It is conceivable that the decrease under certain circumstances may be lessened, but there is a decrease nevertheless. However, under the circumstances described in this case, where every packer had a large fig inventory carry-over, and therefore there was an oversupply, it is difficult to see, as a matter of elementary economic principles, how the fact that the fig industry

may be volatile or speculative is going to cause an increase in value in figs over two years old.

The conclusion is inescapable that neither the existence nor the non-existence of an abnormal fig inventory carry-over, or even the fact that the industry is volatile and speculative, alters the fact that the normal, ordinary and prudent business practice was not to store figs over two years. Since the record is uncontradicted that Arnold did violate this normal practice by having in inventory storage over 6 million pounds of 1954 and 1955 crop figs. (Defs. Exh. S) on June 30, 1957, it was clearly erroneous to conclude that Arnold was not negligent. Accordingly, the judgment that Arnold was not negligent in performing his duties must be reversed.

The argument made by Arnold in attempting to explain why he made such excessive fig purchases (Appellee's Br., pp. 22-24) is, of course, no answer to why he did not dispose of the figs within the two year period once they had been acquired.

The fact that there were high foreign fig imports while Arnold was making excessive purchases only served notice on Arnold that the market was oversupplied, and that he could not expect any increased demand for figs two years or older. Their market value would only decrease as they aged.

The quoted testimony of Herbert Cummings on page 25 of Arnold's brief merely reflects sound principles of economics. If you are selling large quantities of figs you sell them as quickly as possible in order to

prevent the increased supply from decreasing the value of the figs that might be sold later.

3. Rosenberg sustained losses as a result of Arnold's failure to dispose of the old crop fig inventory.

As noted above, the evidence is clear that figs stored over two years decrease in market value, and that such a decrease resulted in a loss to Rosenberg.

The evidence offered to support the loss was the audit report of F. W. Lafrentz & Co. confirming the fact that the sale of the old fig inventory resulted in a loss. (Plts. Exh. 213.) In addition, Rosenberg introduced Defendants' Exhibit AE, a Copy of Agreement Between Rosenberg, Bonner and Roeding, dated April 21, 1958, by which Rosenberg sold a major portion of its old fig inventory to Bonner Packing Co. and Roeding Fig Company. This contract showed the price paid for old figs by type and crop year. The circumstances surrounding this sale are fully set out in the transcript (at pages 565-571). The disposal of the remaining figs not fit for human consumption was made to a distiller of industrial alcohol for $27 a ton. (Tr. 568-569.)

The loss incurred by Rosenberg as a result of the disposal of the old inventory figs was calculated by following normal accounting procedures, i.e. subtracting the proceeds of the sale from the inventory values attributed to the figs on Rosenberg's books.

There can be no doubt that a loss was sustained. As has been pointed out above, it is universally agreed that figs stored over two years decrease in market value. Consequently, a loss will result from what

could have been realized by their sale at an earlier time. In view of the fact that on April 5, 1958, there were on hand over six million pounds of figs over two years old (Defs. Exh. S), the loss is a substantial one, and sufficiently certain for computation.

See:

Hanlon D & S Co. v. Southern Pac. Co. (1928) 92 Cal. App. 230, 235;

Smith v. Shasta Electric Co. (1961) 190 C.A. 2d 728, 732.

See also:

Shannon v. Shafter Oil and Refining Co. (1931) 51 F. 2d 878, 881;

Kelite v. Binzel (1955) 224 F. 2d 131, 144-145.

4. The discussion in Appellee's Brief with regard to evidence of bad fruit inventory is not relevant to the issues on this appeal.

The evidence is clear and unequivocal that there is a lessening in the market value of the bad inventory figs stored for over two years. The evidence is further uncontradicted that Arnold was responsible for keeping old crop figs for periods in excess of two years and that when such old crop figs were sold, Rosenberg suffered a loss because the excessive storage period resulted in a decrease in market value.

5. The cases of Thomas Fruit Co. v. Stuart (1895) 107 Cal. 206 and Rosener v. Hanlon Drydock, etc. Co. (1925) 71 Cal. App. 767, define the standard care required of Arnold and are controlling.

The attempt by Arnold to distinguish the *Thomas* case on the ground that it involved an independent

contractor relationship and not an employer-employee relationship is not a valid distinction since the Court in rendering its decision made no such distinction that plaintiff was negligent in performing its contract.

Arnold tries to make a distinction on the grounds that in the *Thomas* case, plaintiff was required to perform "in a first class manner". This is not a distinction but a point of similarity. Just as plaintiff in the *Thomas* case agreed to perform "in a first class manner" so Arnold in this case agreed to "devote his best efforts to the performance and discharge of his duties" and to "promote the best interests and welfare of Rosenberg". (Tr. 11.) Although the words are different in kind, there is little doubt that in substance they express the same intention, that is, Arnold was to perform in a "first class manner".

Arnold's efforts to distinguish the case of *Rosener v. Hanlon Drydock Etc. Co., supra,* are not clear, but he appears to be saying that there are not standards of care that Arnold was required to follow. This point falls of its own weight in the face of the uniform and uncontradicted evidence by the four experts that it was not normal practice to store old crop figs for periods in excess of two years.

6. **There is no evidence that Arnold did an excellent job after May 7, 1957 until the time of discharge, April 1, 1958.**

The critical period involved in Arnold's performance occurred from May 7, 1957 to April 1, 1958, the time of his discharge. There is no evidence cited by Arnold that anyone was of the opinion he *was* doing a good job during this period.

7. The trial Court manifestly did not apply proper legal principles.

Appellants in their Opening Brief pointed out with specific references where and in what manner the trial Court failed to apply proper legal principles. These references appear in the Opening Brief on pages 25, 33, 42 and 51.

Appellee argues that the trial Court did not apply improper legal principles because the dried fruit industry was "highly competitive, volatile and speculative". This argument was previously discussed above (pp. 17-20), and answered.

8. Arnold had discretion to sell his figs to Rosenberg.

The contract terms clearly provide that Arnold has "discretion" to sell his figs to Rosenberg. (Appellants' Op. Br., p. 37.) Arnold now argues that the word "discretion" was intended only to give Arnold authority "to fix the time where the 'offer' to sell at a specific price would formally be made each year."

This argument points up better than anything else how Arnold was in breach of his fiduciary duty to the corporation. If the argument is correct, then Arnold had it within his power to fix a time to sell his figs to the corporation when he could get the highest price for his figs. Therefore, if the contract is to be interpreted as contended by Arnold, his personal interests in selling his figs to the corporation were adverse to those of the corporation, and if he in fact did sell his figs to the corporation, he was in breach of his fiduciary duty.

Arnold's adverse interest is established without contradiction by Defendants' Exhibit F. the Recap. of 1956 and 1957 Crop Fig Purchases, July 1, 1957 to April 5, 1958. The base price per pound of the figs paid by Rosenberg is compared with what Arnold sought to charge for selling his figs as follows:

"Adriatics	1957 Crop	Pounds	Base Price"	Arnold's Price
Albert Arnold		37,910	.07½"	8¢
"Blacks	1956 Crop			
Albert Arnold		154,145	.05½"	7¢
"Blacks	1957 Crop			
Albert Arnold		391,879	.06¼"	7¢

It is no wonder that Arnold did not want to reach any agreement with Mr. Richard Guggenhime with regard to selling his figs to another packer, since he could never be in a position to pick the best price as he could when selling his figs to Rosenberg.

9. **The policy of the Rosenberg Board of Directors was clear that Arnold was to institute a program of capital reduction, sale of inventories and to buy only what was needed.**

There was no confusion with regard to the policies of the Rosenberg Board of Directors or with the role of Nathan Cummings, as a member of that Board. Furthermore, it was clear to all concerned that Nathan Cummings was the most influential and powerful member of the Rosenberg Board, since he was the representative, as well as Chairman of the Board of the sole stockholder of Rosenberg, Consolidated Foods Corporation.

Arnold was perfectly aware that he was employed in his position after receiving approval from Nathan

Cummings. Nathan Cummings made clear at the Rosenberg Board of Directors' meeting on September 30, 1957 that it was to be the policy of the Board to institute a program of capital reduction and sale of inventories by December 31, 1957, and that if any member of the Rosenberg Board did not agree with these policies and objectives, "he (Nathan Cummings) would simply have to accept that member's resignation." (Plts. Exh. 146, pp. 249, 250, 254.)

No board member resigned and, therefore, the policies so set forth at that meeting by Mr. Nathan Cummings were accepted without a dissent by all the members. It is difficult to find more positive evidence of a policy of a board of directors than that expressed at the Rosenberg September 30, 1957 meeting.

Arnold attempts to show that he cooperated with the Board policy that the company "will not actually acquire" Arnold figs (Defs. Exh, N, p. 190), by relating a conversation with Mr. Richard Guggenhime. (Appellee's Br., pp. 44-45.) However, the record shows (Tr. p. 178) that all Arnold did to sell figs was to have Mr. Hoover, the sales manager, contact the prospective purchaser. He did not approach either Roeding Fig Company or Bonner Packing Company, the very firms that eventually bought Rosenberg's figs. Failure to contact these latter two firms to comply with the board's policy can hardly be regarded as diligent performance of one's duty.

The minutes are clear that Arnold did not advise the board or seek their approval of his sales of his figs to

Rosenberg, and they are further devoid of any statement to the effect that Mr. Guggenhime or any other board member approved the purchase of Arnold's figs. Accordingly, the uncontradicted documentary evidence, which was recorded almost simultaneously with the events, so contradicts Arnold's alleged conversation with Mr. Guggenhime as to make it not probative.

10. Arnold's purchase of his own 1956 natural dried Kadotas establishes that Arnold breached his fiduciary duty to Rosenberg because he caused Rosenberg to purchase figs that were less merchantable than those that could have been purchased.

In our Opening Brief (pages 42-44), we set forth that, by purchasing *his* 1956 crop natural dried Kadota figs, Arnold caused Rosenberg to purchase what he regarded as a less merchantable fig than the tray-dried Kadotas. The evil of this purchase lay in the fact that Arnold was able to cause Rosenberg to purchase his own figs, which he admitted were not as merchantable as others he might buy. In other words, his interest as an individual fig grower and seller was adverse to and in conflict with his interest as the President of Rosenberg. This is a breach of his fiduciary duty and grounds for dismissal.

11. Arnold breached his fiduciary duty to the corporation in selling his own figs to Rosenberg and in concealing the purchase of his figs from the Board of Directors.

In general, Arnold does not quarrel with the legal authorities cited by us in the Opening Brief. A review of the rules and their application to the facts demonstrates that this position is erroneous. See *Pepper v. Litton,* 308 U.S. 295.

Arnold has in three instances manipulated the affairs of Rosenberg and used his strategic position for his own preferment.

First, Arnold had discretion to sell his figs to the corporation at a time he chose. This meant that he had the power to pick a time when the market price was highest. Arnold in fact exercised this power when he sold his 1956 crop figs to Rosenberg in 1957 and claimed top market prices for them. Arnold thereby used his position in preference to the corporation.

Secondly, Arnold caused the corporation to purchase his 1956 crop natural dried Kadotas which were less merchantable than other figs available. Arnold again used his position to obtain a preference for himself.

Third, Arnold failed to disclose to the Board of Directors, which had adopted a policy to control commodity purchases, the fact that he purchased his own figs in the 1957-1958 fiscal year, and which gave him a preference, and prevented the Board from protecting the corporation. The facts supporting this point are outlined on pages 30-32 of this Brief.

The evidence makes it abundantly clear that Arnold's transactions with Rosenberg with regard to the sale of his figs were not arm's-length transactions, but in fact tainted with personal preference for Arnold and therefore void, and grounds for dismissal.

12. Board directives.

Appellee Arnold's contention that there were no board directives which he failed to obey was fully answered in Appellant's Opening Brief, pages 51-60.

Any argument that Mr. Nathan Cummings' statements at board meetings were not board policy is foreclosed by the following excerpt from the minutes of the August 27, 1957 meeting (Plts. Exh. 181, p. 217):

> "*The Chairman commented that when Mr. Nathan Cummings asked specifically at the recent Board meetings if the Board had approved projected 1957 crop purchases, commodity by commodity, it was evident that the Board must shoulder this responsibility and therefore had to keep a very close check on the purchase program.* Mr. Drew concurred but said that actually the Board did assume this responsibility at the Fresno meeting. The Chairman then stated that the parent company has set up an objective and that consistent with that objective, he wants to do all he can to assure the company's continued operation." (Emphasis added.)

It is clear from this statement that the other members of the Board regarded the statements of Mr. Nathan Cummings as Board policy.

III

APPELLANT'S COUNTERCLAIM.

The argument with regard to Appellant's Counter-
laim is fully set out in the Opening Brief and ade-
uately answers the vague point made by Arnold.

IV

RECOVERY OF INTEREST ON PROFITS.

In view of the fact that Arnold has failed to prove
hat Arnold-Hoover, Inc. realized any profits, the
uestion of interest does not arise.

CONCLUSION

In light of the reasons set forth herein and in Ap-
ellant's Opening Brief, the judgment of the trial
'ourt that plaintiff is entitled to $23,677.40, rep-
esenting 50% of the alleged profits of Arnold-Hoover,
nc., and $112,500 in unpaid wages with interest be
eversed.

It is further respectfully submitted that this Court
hall instruct the trial Court to enter findings of fact
nd conclusions of law that plaintiff was negligent in
ıe performance of his duties, that he did breach his
duciary duty to Rosenberg, and that he did disobey
ıwful policies of the Board of Directors, all of which
onstituted good cause for discharge, and that Arnold

be denied recovery for his wages or profits and furthe[r] that the trial Court should be instructed to determin[e] what if any damages were caused Rosenberg b[y] Arnold's negligence and breach of his fiduciary duty

Dated, San Francisco, California,
August 27, 1963.

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CERTIFICATE OF COUNSEL

I certify that, in connection with the preparation o[f] this brief, I have examined Rules 18 and 19 of th[e] United States Court of Appeals for the Ninth Circuit and that, in my opinion, the foregoing brief is in ful[l] compliance with those rules.

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